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July 23, 1999


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FEDERAL COMMUNICATIONS COMMISSION
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**HAND DELIVERED**

Magalie Roman Salas, Esq.
Secretary
Federal Communications Commission
445 Twelfth Street, S.W.,
Washington, D.C. 20554

Re: CC Docket No. 96-45, CC Docket No. 96-262

Dear Ms. Salas:

Transmitted herewith, on behalf of TDS Telecommunications Corporation (TDS Telecom or TDS), are an original and six copies of its comments in response to the Federal-State Joint Board on Universal Service, CC Docket Nos. 96-45 and 96-262.

In the event of any questions concerning this matter, please communicate with this office.

Very Truly Yours,

Margot Smiley Humphrey

Margot Smiley Humphrey

Enclosure

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**Before the**
**Federal Communications Commission**
**Washington, D.C. 20554**

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| In the Matter of | ) | |
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| Federal-State Joint Board on Universal Service | ) | CC Docket No. 96-45 |
| | ) | |
| Access Charge Reform | ) | CC Docket No. 96-262 |

**COMMENTS OF TDS TELECOMMUNICATIONS CORPORATION**

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## TABLE OF CONTENTS

**Before the**
**Federal Communications Commission**
**Washington, D.C. 20554**

| | | |
|---|---|---|
| In the Matter of | ) | |
| | ) | |
| Federal-State Joint Board on Universal Service | ) | CC Docket No. 96-45 |
| | ) | |
| | ) | |
| Access Charge Reform | ) | CC Docket No. 96-262 |

**COMMENTS OF TDS TELECOMMUNICATIONS CORPORATION**

TDS TELECOMMUNICATIONS CORPORATION (TDS Telecom), by its attorneys, submits these comments on the Further Notice of Proposed Rulemaking portion of the Commission's recent decision in the above captioned proceedings.[1] TDS Telecom owns 105 incumbent local exchange carriers (ILECs) in 28 states. All of the TDS Telecom ILECs qualify as "rural telephone companies" under section 3(47) of the Telecommunications Act of 1996.[2]

## I. Introduction and Summary

The Commission has wisely decided to tackle high cost support issues for rural carriers in a separate, later proceeding, after the Rural Task Force has made a recommendation to the Joint Board. Differences between rural and non-rural companies and among rural carriers thoroughly

[1] Seventh Report & Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45; Fourth Report & Order in CC Docket No. 96-262 and Further Notice of Proposed Rulemaking, FCC 99-119 (rel. May 28, 1999) (FNPRM).

[2] The 1996 Act amended the Communications Act of 1934, 47 U.S.C. § 151, *et seq*. *See* Pub. L. No. 104-104, 110 Stat. 56 (1996).

justify separate consideration, and TDS Telecom urges the Commission to view the issues addressed here on the basis of non-rural market characteristics from a genuinely fresh perspective when it considers rural issues anew. Indeed, the complexity and inaccuracies of proxy efforts so far are themselves reasons not to prejudge the cost methodology appropriate for rural carriers by what might be adopted for large carriers.

The geographic area for averaging costs should not be chosen with the motive of preventing support from increasing, since the statute requires "sufficient" support. For rural carriers, an assumption that current support should not be increased is further prohibited by the legal mandate for reasonably comparable rates, services and access to advanced telecommunications and information services. Study areas are suitable for measuring costs and total support needs for rural companies, but support needs to be disaggregated to reflect cost variances within study areas. Otherwise, portability will distort entry signals, disturb the balance between the costs to serve different customers and the support available for such service and create windfalls for unregulated entrants, while the incumbent is left with the highest cost customers and insufficient support.

Measurements of state ability to support some high costs must be carefully crafted to prevent undue burdens on high-cost states and rural subscribers, which would conflict with the nationwide support mandate of section 254. The lines "counted" to judge ability to support a per-line amount must include competitors' lines. Otherwise, the most commercially attractive markets and states will appear to be the least able to generate internal state support. Moreover, a "hold harmless" by state that caters to the notion that states provide or receive net support flows under a national plan ignores the nationwide consumer interests that drove Congress and instead favors state jockeying that the law does not authorize. A carrier-based hold harmless follows the law by targeting "predictable" support to carriers as section 254(e) dictates, and advances the intention of safeguarding customers throughout the nation.

Portability, use of an imaginary cost proxy and treating even low-cost out-of-area UNEs as "owned" high-cost facilities compound the difficulty of enforcing the legal requirement that support be used only for universal service purposes. The Commission must not allow support ultimately provided by end users to be wasted by paying for non-high-cost situations.

## II. The Commission Should Continue to Confine This Phase of its Proceedings and Any Resulting Determinations about High Cost Support to Non- Rural Carriers

The FNPRM poses questions about specific methodological issues related to the universal service mechanism the Commission is developing for "non-rural" carriers. Commissioner Ness, Chairman of the Federal State Joint Board on Universal Service, reaffirmed the limited scope of this proceeding in her opening remarks at the May 27, 1999 meeting adopting the FNPRM and again in her separate statement dated June 18, 1999 (pp. 1-2). Commissioner Ness made it clear that this phase of the universal service reform proceedings does not include questions about what high cost mechanism is appropriate for rural carriers, explaining that:

> Nothing we do today implicates rural carriers. The Telecommunications Act is clear that we should not hamper the ability of rural telephone companies – some 1300 strong – to serve their communities. Thus, the Joint Board established a Rural Task Force to examine the unique circumstances of rural carriers. I ... want to assure rural carriers that I will not support changes in their funding mechanisms until we have consulted with the Rural Task Force and are satisfied that the changes make sense for small rural carriers.

TDS Telecom agrees with the Commission and the Joint Board that the issues raised by providing universal service in the high cost areas served by small and rural companies should be considered on their own. The decision to compile a separate record and analysis before adopting a different universal service mechanism for rural telephone companies will properly enable the Joint Board and the Commission to take into account the wide divergences in characteristics between rural telephone companies and the non-rural companies under consideration here, as well as the variances among rural telephone companies. TDS Telecom is attentively following the Rural Task Force's exploration of the issues raised by service to companies with small customer bases, low density service areas, or insular locations.

It is important for the future proceeding to evaluate universal service reform proposals for areas served by rural telephone companies to be truly separate -- without any prejudgment or carryover of decisions made here on any issues, including whether a proxy cost model can be appropriate. What TDS Telecom has seen of the proxy models under development so far has reinforced the indications that a proxy model will never work with sufficient accuracy for these areas to justify using such as model to calculate their costs. Indeed, the complexity and time necessary to run the current proxy provide strong additional reasons not to commit achievement of the rural principles in section 254(b) to such an unpredictable, non-company-specific and unwieldy process. For these reasons, TDS Telecom will not comment on issues such as what should be the range and level for a benchmark to be used with the non-rural proxy.[2]

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[2] TDS Telecom has consistently taken the position that any high cost mechanism should work with a cost rather than a revenue benchmark. Thus, shifting to a cost benchmark for non-rural companies seems to be a positive step.

## III. The Determination of What Area To Use for Cost or Support Averaging for Rural Telephone Companies Involves Different Considerations from the Non-Rural Issues Raised in the FNPRM

The Commission is exploring (paras. 108-109) at least four alternatives for deciding what area it should adopt for calculating non-rural company costs. The Commission admits that competition will make study-area-wide averaging increasingly unsustainable, but nevertheless proposes to consider broad enough geographical averaging for non-rural ILECs' costs to achieve its stated objective of preventing total universal service support from increasing. TDS Telecom has no way of knowing whether the Commission's alternatives will generate "sufficient" support to achieve the section 254 principles in non-rural carriers' areas. However, the Commission's reasoning that current rates are "affordable," so current support is "sufficient" lacks record or logical support for rural carriers' areas. A similar goal of preventing support from increasing in rural carriers' areas, based on presuming current rates satisfy section 254, would be totally unjustified because rural rates have to meet an additional criterion under the Act besides remaining affordable: Rural rates and services must be "reasonably comparable" to those in urban areas. Only when the non-rural universal service mechanism is completed and implemented and access reform for price cap carriers is factored in will information about the resulting levels of local rates and SLCs in urban areas become available. That information will be essential to applying the comparability standard for rural areas in the later proceeding dealing with high cost issues for rural carriers.

Section 214(e) prescribes the study area as the service area for rural telephone companies for universal service support purposes, unless a statutory change procedure is completed.[3] The study area should, accordingly, be used to define the universal service responsibilities of any additional eligible telecommunications carrier designated in a rural telephone company's area, unless it has been changed pursuant to the requirements in the law. TDS Telecom believes that the study area should also be the area for determining costs for rural carriers.

However, since rural carriers' costs of service differ in different parts of their study areas, the distribution of support within their study areas should not be averaged. Unless support is disaggregated for distribution in a more targeted fashion, the availability of portable study-area-average support for lines that cost less to serve than the study area average will create perverse entry incentives for competing carriers. Such carriers are able to choose where to serve with facilities and where to serve by reselling the ILEC's above average cost lines and taking advantage of the high cost support built into the ILEC's rates. When that occurs, the ILEC loses the study-area-average per-line support, but retains the higher cost customers. The resulting shortfall in ILEC support for the highest cost customers would increase the costs the ILEC would have to recover in local rates from those same customers whose service is the most costly to provide.

## IV. The Commission Needs to Reexamine its Reasons and Proposals for Determining Each State's Ability to Provide Support Internally

The Commission has decided (para. 63) to measure each state's ability to support its universal service needs. Reasoning that a state is better able to recover high costs to the extent

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[3] See, 47 C.F.R. § 54.207.

that it has more lines over which to spread the cost and that a percentage of state revenues would not be a reliable test of the state's ability, the Commission has also decided (paras. 63-64) to adopt a fixed amount per line. Each state will then multiply the fixed per-line amount by the number of non-rural company loops in the state (para. 66). Although it is not entirely clear, it appears that the fixed amount a state is deemed to be able to support internally will be the same nationwide. If that is the proposal, it is essential that the nationwide per-line support left for states to cover be kept small enough to avoid putting an undue high cost recovery burden on customers within the highest cost states.

The Commission now plans to determine what that fixed amount per line to be recovered within each state should be (para. 111) and which lines should be taken into account when the fixed amount is multiplied by the state non-rural company lines (para. 112). The Commission's paramount concern must be that the resulting nationwide support is "sufficient." Rural customers in states without large urban markets and large populations to help defray universal service costs cannot lawfully be put at a disadvantage with rates and services that do not meet the "reasonably comparable" standard. TDS Telecom cannot comment on the impact of various fixed amounts on non-rural companies, their customers, or their states, and consequently will wait for the rural carrier proceeding to participate fully in the de novo exploration of issues and mechanisms for these unique markets. However, TDS Telecom cannot forego the general observation that the Commission and the Joint Board are courting judicial reversal by basing federal decisions about a nationwide support mechanism to generate "sufficient" support for rates and services for customers in high cost areas on parochial state disputes about what states are "winners" and "losers." A nationwide support mechanism involves nationwide customer interests, not

The Commission must find a way to ensure that ratepayers nationwide will not be forced to fund portable support payments based on imaginary model costs, when such support will not demonstrably be used only for statutory universal service purposes, while insuring that support is adequate for truly high-cost rural service; and

The Commission must maintain the consumer-centered focus Congress intended by adopting a hold harmless by carrier to satisfy section 254(e) and refraining from substituting an unauthorized state-by-state approach to curb fund growth for the legally required result -- sufficient support.

Respectfully submitted,

**TDS TELECOMMUNICATIONS CORPORATION**

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By: /s/ Margot Smiley Humphrey
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July 23, 1999

## CERTIFICATE OF SERVICE

I, Victoria C. Kim, of Koteen & Naftalin, hereby certify that true copies of the foregoing Comments of TDS Telecom on Access Charge Reform, CC Docket Nos. 96-45 and 96-262, have been served on the parties listed below, via first class mail, postage prepaid on the 23rd day of July 1999.

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individual state interests, for which the 1996 Act provided in section 254(f). For federal support purposes, state boundaries are transparent and irrelevant.[4] Assuming that the Commission nevertheless goes forward with its efforts to manage state-to-state support flows, it must not let that consideration get in the way of satisfying the requirements of section 254.

So long as the support provided for the customers within every state is "sufficient" under section 254, it makes sense to consider all the lines used by all carriers to provide local service directly to end users in that state in determining a state's ability to pay. As competition develops, counting the lines of only one of the carriers providing local service will provide an increasingly meaningless number. If only ILEC lines are counted as customers increasingly use CLEC or wireless for ILEC service, states where the marketplace stimulates the most competition will appear to be less able to support universal service internally by spreading costs over a large number of lines.

## V. The Commission Should Promulgate Rules that Ensure the Use of Support for the Statutory Purposes

TDS Telecom agrees that the Commission should ensure that support is only used for the provision, maintenance, and upgrading of facilities to provide the "evolving" universal services that section 254 requires. The Commission's commitment to develop a proxy model to identify what high costs require support creates a whole new set of problems in ensuring that the support

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[4] It is also a mystery why only high-cost support is "counted" by states in this non-statutory wrangling over "payer" and "receiver" states. Information released by House Telecommunications Subcommittee Chairman Billy Tauzin in opposition to the Commission's increase in funding for the schools and libraries programs under section 254(h) showed, for example, that New York, one of the NARUC Communications Committee's strongest apologists for limiting its "outflow" of high cost support was this year's third largest beneficiary of these (imaginary) state-to-state e-rate transfer payments.

received is used for the purposes Congress intended. Historically, support was based on the actual investments and expenses of each incumbent local exchange provider. Moreover, under traditional cost recovery mechanisms, the costs of universal service in high cost areas had already been incurred before they were calculated or compensated by universal service support.

The Commission is designing a cost proxy model that will predict the forward looking costs of an imaginary efficient carrier to provide the services within the definition adopted pursuant to section 254 to all the customers within a given area on a monopoly basis. Consequently, there is an unavoidable logical gap between the proxy costs on which support will be based and the costs of the actual network provided by any real-life carrier because a proxy model does not use actual costs that carriers have incurred to meet statutory obligations. The problem is even greater when competitive entrants become ETCs because of the Commission's decision to treat UNEs they obtain from ILECs as their "own" facilities, eligible for support up to the full payment for the UNE, even if the capability is obtained from an ILEC outside the high cost area for which the competitive ETC (CETC) has been designated as eligible for support. The daunting challenge of tracking how such support is used without even knowing the costs of service actually incurred by CETCs adds to the conundrum.

In addition, while support remains averaged on a study area basis, a CETC will have the incentive to use facilities only to serve customers in those parts of the study area where its costs are less than the study area averaged per line support it will collect. Elsewhere, it will have the incentive to resell the ILEC's lines, which it will secure at below-cost, supported rates in the higher cost portions of the study area. Although using resold service will not switch support payments to the CETC, a CETC's resulting above-average support for providing service at below-average cost cannot be justified under the section 254(e) use-of-support standard.

Indeed, until (a) the existing portability rules are modified to answer the questions in the letters submitted in February and July by the Universal Service Administrative Company (USAC) and (b) rules are developed to answer other open questions, it is not even clear what lines are eligible for support. Currently, there are no rules about what rates a CETC may charge or how to tell if it is providing below-cost service. It is not clear how to tell what lines are eligible as "captured" from an ILEC, provided as new lines to previously unserved customers or merely existing lines that were provided without support in response to marketplace forces before the providing carrier became a CETC. Hence, CETCs may not even <u>know</u> whether they are using the support they receive for the intended purposes, as section 254(e) requires. The Commission needs to figure out a reliable method to track support to CETCs to prevent customers and carriers throughout the nation from providing support that is retained as profit or used for other purposes than universal service.

## VI. "Hold Harmless" Should Apply on a Carrier Basis, Not to Each State for the Aggregate Amount Its Carriers Received

Section 254(e) requires a federal universal service mechanism that provides "sufficient" and "predictable" support. The Joint Board and the Commission have decided on a hold harmless provision in the non-rural carrier support mechanism, which TDS Telecom endorses as a prudent decision. However, the Commission is now looking at whether to apply the principle to maintain each state's total support from the nationwide federal program or to maintain each carrier's support for the lines that carrier continues to serve. Although the Commission has not yet begun to consider a rural carrier high cost mechanism, TDS Telecom offers a few observations about the non-rural "hold harmless" issues raised here.

There is no statutory basis for measuring sufficiency or distributing support on the basis of the aggregate support paid to each state's carriers. In the first place, section 254(e) plainly provides that support will be paid to carriers designated under section 214(e). Section 214(e) authorizes each state to designate ETCs and service areas for universal service purposes, but does not authorize any delegation of the Commission's authority or responsibility to provide for "sufficient" and "predictable" federal support to any state.

The Commission's main reason for considering a hold harmless for each state instead of for the company providing universal service is also statutorily suspect. The Commission points out (paras. 69-70) that a using hold harmless by state can hold total support to lower levels than a hold harmless by carrier because states will be able to reduce individual carriers' support levels. A critical problem with this plan is that it undercuts the only rationale the Commission has suggested for its belief that universal service funding need and should not rise materially above current levels -- its conclusion that rates are currently affordable, so current support must be sufficient. The Commission cannot simply assume from the conclusion that rates are currently affordable for all non-rural carriers' customers today, however, that those carriers' rates will be affordable and reasonably comparable for their rural and urban customers if each state is free to modify the current level of presumptively sufficient support for any company. Nor can the Commission satisfy the 1996 Act's requirement for support that is "predictable." If each of fifty states is able to redirect today's aggregate Federal support within that state, neither the

Commission, the carriers nor customers can count on the predictable support Congress intended under section 254. TDS Telecom recognizes that the Commission told Congress in its May 8, 1998 report that it would not provide any less federal support for any "state." However, that was before the Commission had come to the conclusion that support should not increase. The use of a hold harmless based on the support for each carrier will (subject only to problems caused by unresolved portability issues) enable the carriers to maintain rates at present levels and keep the Commission's promise to maintain each state's level of support.[5]

## VII. Conclusion

The Commission should honor its commitment not to consider rural carrier universal service issues now by bringing a truly fresh perspective to its later rural carrier proceedings, especially since proxy efforts thus far have not indicated an ability to deal with the pervasive differences that set rural carriers apart. Therefore, the Commission should keep the following points in mind as it considers non-rural support, but even more so when it comes later to rural carrier issues:

It should beware of geographic averaging to keep the fund from growing even for non-rural carriers, owing to the mandate for sufficient support, recognizing that size control is not a valid consideration for rural carrier areas until the mandates for sufficiency and reasonable rural and urban comparability have been satisfied on the basis of a rural record;

Sufficient support must also take statutory precedence over imaginary support "flows" from state to state, and tests of states' ability to provide internal support must not overburden rural states or their residents and businesses;

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[5] TDS Telecom will not comment in detail on the Commission's proposal that non-rural carriers should deduct from their access charges whatever amount implicit support is removed from access charges. However, the Commission should keep in mind the statutory mandate for geographic toll rate averaging in section 254(g) and make sure that its universal service and access charge reforms do not result in deaveraging and inadequate support to sustain geographic toll rate averaging.